

A GUIDE TO CONTRACTOR LICENSE BONDS

What is a Surety Bond?

As a condition of licensure, contractors are required to post some form of security deposit with the Contractors State License Board (CSLB). Surety bonds are commonly used for this purpose, but cash or certificates of deposit may also be posted.

A surety bond is a contract in which a surety company promises the State of California that the contractor will comply with the Contractors' State License Law (CSLL) [Chapter 9 of Division 3 - commencing with Section 7000 - of the Business and Professions (B&P) Code.]

Generally, the contractor's obligation is to not commit any violations of the CSLL that are grounds for disciplinary action against the license. The law describes specific violations that the bond will cover. If the contractor does not comply with the conditions of the bond, a consumer, supplier or an employee may file a claim against the bond. (B&P Code Section 7071.5)

A surety bond should not be confused with an insurance policy since there are important distinctions between the two. One important difference is that the contractor remains liable for his or her own obligations, and must repay the surety for losses incurred by the surety as a result of the contractor's actions.

Is a complaint filed with the CSLB automatically a claim against a bond?

A person may file a complaint with the CSLB without filing a claim against the bond. A person may also file a claim against the bond without filing a complaint with the CSLB. The surety company will investigate any claim filed against the bond, and the CSLB will investigate any complaint filed against the license. Many times, the issues involved in the two matters are related. The CSLB and the surety company will independently resolve the issues under their respective jurisdictions. The surety company will determine if it will pay the claim, and the CSLB will decide if disciplinary action or some other resolution of the complaint is appropriate.

What incentive does the contractor have to resolve the problem with the complainant?

If a surety company pays a claim on a contractor's bond, the surety is required by law to report the loss payment to the CSLB. The contractor is obligated to reimburse the surety for any loss payment from the bond. The surety may also cancel the bond, and the CSLB may suspend the contractor's license until the surety is reimbursed. A payment from the bond could affect the contractor's license and livelihood.



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What is the amount of the required bond?

The amount of the contractor's license bond is \$12,500 as of January 1, 2007. [*Business and Professions (B&P) Code Section 7071.9*].

The bond amount is not per job—it is the amount available for all the jobs a contractor takes on during the life of the bond. In addition, the CSLB may require a separate bond for contractors who have been disciplined, and the amounts of these bonds vary.

Once the bond has been depleted, a contractor must purchase a new bond for the license to remain in effect.

Who is protected by a Surety Bond?

Persons who can make a claim against the bond are listed in the CSLL (*B&P Code Section 7071.5*), and include:

- A. Any homeowner contracting for home improvement work on the homeowner's personal family residence that is damaged as a result of a violation of the CSLL by the licensee;
- B. Any person damaged as a result of a willful and deliberate violation of the CSLL by the licensee, or by license fraud in the execution or performance of a construction contract;
- C. Any employee of the licensee damaged by the licensee's failure to pay wages; or
- D. Any express trust fund damaged as a result of the licensee's failure to pay fringe benefits for eligible employees.

What can a contractor do to avoid a claim against a bond?

To limit the likelihood of a claim being filed against a bond:

- A contractor should always put the terms of a construction contract, and any amendments, in writing.
- A contractor should maintain accurate records of all funds paid and received, and confirm in writing any agreements reached if the project is terminated.
- A contractor should communicate frequently and effectively with project owners and prime or subcontractors regarding any potential or actual problems.

Many claims against the bond are filed by subcontractors and suppliers for nonpayment of invoices. These claims can often be avoided by communicating with the suppliers, making them aware of circumstances that may have prevented payment, and proposing a reasonable plan to pay. Business associates are more inclined to make reasonable arrangements when they are kept informed of unusual circumstances.

How does a consumer file a claim against a bond?

- Consult the CSLB's Website for information about the bonding company that wrote the surety bond covering the dates of the contract and the dates of the construction.

- Contact the surety company, providing it with a detailed written description of the problem and attaching a copy of the contract and all other pertinent documents and information.
- If a consumer is not satisfied with the response of the surety company, they may take the contractor and the surety company to Small Claims Court for amounts of up to \$7,500 (claims against the surety company are capped at \$4,000). Claims above \$7,500 must be filed in Superior Court. Code of *Civil Procedure Section 116.220(c)* CSLB's publication, *A Consumer Guide to Filing a Small Claims Court Construction Claim* provides additional information.

What is the time frame for an action to be filed against a bond?

Any action other than one to recover employee fringe benefits must be filed within two years after the expiration of the license period during which the act or omission occurred, or within two years of the date the license was inactivated, canceled, or revoked by the CSLB, whichever occurs first.

What should a contractor do if a claim is filed against his or her bond?

If a contractor receives a notice from a surety company that a claim has been filed against his or her bond, the contractor should immediately contact the surety to respond to the claim and explain in detail his/her position. The contractor should also submit all documentation relevant to the claim. If a complaint was filed with the CSLB, the contractor should respond immediately and fully to the complaint and provide the CSLB all requested information for the duration of the investigation. Both the CSLB and the surety take complaints very seriously, so cooperation is important for a full understanding of the facts.

What if there are a number of claims filed against the bond?

If the amount of the bond is insufficient to pay all claims in full, the bond amount will be broken down and distributed to all claimants in proportion to the amount of their respective claims, with priority to claims for wages and fringe benefits.